

GAO

Testimony

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Statement of
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Mr. Chairman and Members of the Commission, we are pleased to appear today to discuss the issue of contracting out for commercial activities, as outlined by Office of Management and Budget (OMB) Circular A-76. Current government policy requires executive branch agencies to procure commercial goods and services from private sector sources when they can accomplish the same quality job at less cost than a government operation. Inherently governmental functions, however, must continue to be performed by federal employees.

The A-76 program remains controversial. Proponents believe it can achieve substantial savings and improve government productivity. Others are concerned about its effect on quality of services and its potential impact on federal managers and employees.

Decisions over who--government employees or private contractors--should provide needed services are always likely to be subject to much debate. There are inherent difficulties in weighing the various factors which need to be considered in arriving at such decisions. However, it is both reasonable and good management practice to reassess the government's activities to determine what the most effective and economical ways are to obtain goods and services. This should be done with the clear recognition that the process for making such decisions should be continually examined to ensure it is as credible as possible.

We have made numerous reviews of the A-76 program over the years, and have examined the work of others. While these studies addressed a wide range of issues, there are two I would like to focus on today: the difficulties in implementing the process and the impact of the A-76 program on federal employees.

I will briefly expand on each area, drawing primarily on the experiences of the Department of Defense, which has been the most active in implementing A-76. DOD has studied about 56,000 positions. During fiscal year 1986, for example, it completed 180 full cost comparisons affecting 7,000 positions and another 87 direct conversions affecting 1,100 positions. DOD estimates \$86.5 million annual savings from these efforts.

CONTINUING DIFFICULTIES IN
IMPLEMENTING THE PROCESS

Federal agencies or the Congress have not fully embraced the A-76 program. Agencies, in total, have achieved less than one-third of OMB's goals for numbers of positions in activities to be studied in fiscal years 1984 through 1986. While proposals to legislate the A-76 program have been made, the Congress has instead tended to exclude certain activities from the A-76 process.

Experience to date with the A-76 study process provides insight into the difficulties involved in effectively implementing the program. This overall process was designed to help agency decisionmakers select the most economical method of obtaining quality services. However, our past reviews and reports by Defense audit groups show the continuing problems agencies have in implementing the process. These include difficulties in precisely defining the requirements for needed services and in accurately estimating all potential costs.

The A-76 process has several steps which are intended to help ensure reliable estimates and allow affected parties an opportunity to express their views. Once a targeted activity is scheduled for an A-76 study, the government's requirements are to be precisely defined in a Performance Work Statement, or PWS. A management study is also conducted to determine the Most Efficient Organization (MEO) needed to accomplish the tasks in the PWS. The MEO is then to be used to develop the in-house cost estimate, which is to be subsequently compared to bids received from contractors, leading to a decision to remain in-house or to award a contract. Affected parties then can file an appeal as a safeguard to ensure that the decision is equitable and in accordance with A-76 procedures.

A key implementation concern has been adequate development of the PWS. Past audit reports have shown that PWSs have not

always precisely defined all necessary requirements. Task requirements need to be clearly described to reduce the chances for delays and avoid increased costs. Mistakes in the PWS can result in inaccurate estimates of savings.

For example, in a 1985 report we found that in 12 of 20 Defense functions examined, the amount of estimated savings from contracting out was not fully realized. We found that for six of these functions, contract cost increases were caused by errors or ambiguities resulting from inadequate PWSs. Also, in a 1984 report, the Air Force Audit Agency identified six contracts where modifications of almost \$4 million were made as a result of errors in the original work statements. In a 1984 review of commercial activities at 17 installations, the Army Inspector General found that PWSs lacked specificity and were inadequate or incomplete at all but one installation.

Another implementation problem is accurately estimating future contract administration costs. For example, the Naval Audit Service reported in 1984 that in 9 of 11 contract functions it reviewed, projected savings were not realized due to higher than estimated contract administration costs and modifications increasing the scope of work. Similarly, a 1983 Army Audit Agency report stated that the average contract administration costs for 12 contracts it reviewed were more than double the estimates used for the cost study.

There have also been instances of unrealized savings from decisions to go with in-house organizations. For example, in its 1984 report on 25 commercial activities that remained in-house, the Army Audit Agency found that for 8 of the activities, the MEO had not been implemented promptly or in the manner prescribed by the management study. It reported that the costs of in-house operations were higher than projected and operations were not efficient.

EFFECT ON FEDERAL EMPLOYEES

Employees undergoing an A-76 study face uncertainties about their future, which can result in lowered morale and reduced productivity. The process creates anxiety about whether the activity will remain in-house or be performed by a contractor. Employees generally recognize that a decision to contract out may mean a significant career move, or precipitate a change in pay status.

Such anxiety can be heightened by the length of time it takes to complete a study. Our preliminary analysis shows that on average, for the period October 1978 through December 1986, it took about 24 months to complete a Defense study. About 40 percent took more than 2 years to complete, with a few extending from 5 to 8 years.

In the past, we reviewed the effect on federal employees when their activities were contracted out. In 1985 we reported on the effects of contracting out on 2,535 employees: 74 percent found other government jobs, with the majority taking positions at lower grades; 7 percent went to work for the contractor; 5 percent were involuntarily separated; and most of the remaining employees resigned or retired.

We later followed up with those employees who were involuntarily separated or had gone to work for contractors. Of those who responded, over half who had been involuntarily separated said that they had received unemployment compensation and/or public assistance. Fifty-three percent who went to work for contractors said they had received lower wages, and most reported that contractor benefits were not as good as their government benefits.

SUMMARY

In summary, the A-76 program has encouraged competition for providing quality goods and services needed by government agencies. In fact, OMB reported that about half of all A-76 decisions have resulted in remaining in-house, with the other half going to the private sector. The program has reported estimated savings, but in some instances estimated savings have not been fully realized.

Widespread and effective implementation will be difficult to achieve without proper incentives and supporting legislation. Even with such additional support, the process of making decisions on the appropriateness of contracting out for commercial activities is likely to remain contentious. On the other hand, such an examination is needed to help ensure efficient and effective government operations. In making such examinations, a sustained effort should be made to ensure that reliable and timely information is available for informed decisionmaking. In this context, GAO supports the concept of seeking the most economical means to obtain goods and services, and of using the private sector if the same quality of goods and services can be obtained at lower cost, and if it is in the national interest.

That concludes my prepared remarks. We would be happy to answer any questions.

LIST OF RELEVANT GAO REPORTS

<u>Title</u>	<u>Date</u>	<u>Publication number</u>
<u>Development Of A National Make-Or-Buy-Strategy--Progress and Problems</u>	9/25/78	PSAD-78-118
<u>Factors Influencing DOD Decisions To Convert Activities From In-House To Contractor Performance</u>	4/22/81	PLRD-81-19
<u>Civil Servants And Contract Employees: Who Should Do What For The Federal Government</u>	6/19/81	FPCD-81-43
<u>Review of DOD Contracts Awarded Under OMB Circular A-76</u>	8/26/81	PLRD-81-58
<u>Increased Agency Use Of Efficiency Guidelines For Commercial Activities Can Save Millions</u>	9/30/81	FPCD-81-78
<u>Synopsis Of GAO Reports Involving Contracting Out Under OMB Circular A-76</u>	5/24/83	PLRD-83-74
<u>Compendium Of GAO's Views On The Cost Saving Proposals Of the Grace Commission, Vol. II-Individual Issue Analyses, pp. 229-230.</u>	2/19/85	OGC-85-1
<u>DOD Functions Contracted Out Under OMB Circular A-76: Contract Cost Increases And The Effects On Federal Employees</u>	4/15/85	NSIAD-85-49
<u>DOD Functions Contracted Out Under OMB Circular A-76: Costs and Status of Certain Displaced Employees</u>	7/12/85	NSIAD-85-90
<u>Information From Previous Reports On Various Aspects Of Contracting Out Under OMB Circular A-76</u>	7/5/85	NSIAD-85-107
<u>Potential Savings From Private Sector Cost Comparisons</u>	12/31/86	GGD-87-30
<u>Federal Workforce: Legislative Provisions for Comparing Government and Contractor Retirement Costs Should Be Changed</u>	12/17/87	GGD-88-25